A STUDY OF THE 1986 PROPOSED BANKING REFORM IN HONG KONG

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ABSTRACT

Since 1983, the banking industry has gone through some very troubled times. It started with the British and the Chinese Governments' discussion about the future of Hong Kong. Public panic caused by political uncertainty brought turbulence to the local economy. Most people were scrambling for cash or other forms of liquid assets in order to take refuge overseas.

It was at this period that a series of local banks ran into trouble. The first was the Hang Lung Bank, then the Overseas Trust Bank, followed by the Ka Wah Bank, the Wing On Bank and most recently the Union Bank. The occurrence of these events was not incidental. As a result, the existing Banking Ordinance was severely critized for its insufficiency, deficiency and outdatedness, making it very difficult to cope with the rapidly changing banking community.

The Hong Kong Government was well aware of the importance of maintaining a sound and efficient banking system in order to safeguard Hong Kong's image as an international financial centre. A proposed Banking Ordinance Reform was announced in March, 1986, aiming at amending the lopholes in the existing ordinance and to better define the role of the Banking Commissioner.

We began our analysis by looking into the existing ordinance in order to pinpoint lopholes. We then commented on the major changes in the proposed Banking Ordinance. Finally we interviewed bankers of different background, summarized their opinions and comments, and submit our recommendations.

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CHAPTER I

INTRODUCTION

During the past few years, banking industry of Hong Kong has not been in a very good shape. Due to the slump in Hong Kong property market, the amount of bad debts for banks involved in domestic market are quite substantial. In Sept., 1983, a local bank, Hang Lung Bank, suffered a run and became insolvent. The bank was soon taken over by the Hong Kong Government, an unprecendent move derivating from its usual non-intervention policy, in order to resume confidence of depositors. However, fraud was later discovered and some of the directors of the bank were involved. In the High Court on Oct. 18, 1984, it was revealed that a massive cheque-kitting exercise involving US$21.7 billion was a material factor in the ultimate collapse of the bank and Dollar Credit Finance Co., a deposit taking company which was found to be insolvent in November, 1982.[1]

Unfortunately, another local bank with larger asset base, the Overseas Trust Bank, ran into trouble in June, 1985. The Overseas Trust Bank (hereinafter called OTB) is one of the biggest local banks and has 43 branches in Hong Kong and 8 in overseas. The crisis appeared to have been touched off by a fraudulent diversion of funds, similar to the case of Hang Lung Bank and

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[1]Cecillia Ko, "Watchdog that lost its bark," South China Morning Post, Oct. 15, 1985.

Dollar Credit Finance. Worried by potential fallout from the OTB collapse, the Government took over the bank with a cost estimated to be about HK$2 billion. No reasons have yet been given by the Government for the suddent collapse of the bank except that of suspected fraud. Several former shareholders and senior executives were put on trial facing charges of conspiracy to defraud shareholders and creditors of OTB. It was reported that some missing funds, estimated to be as much as HK$2 billion, were loaned to companies controlled by former directors. The insider transactions took place not only in Hong Kong, but also in OTB's offshore branches, mainly Macau and Colombo. In the past few months, a total of 87 writs claiming repayment of almost HK$1.2 billion have been filed by OTB and its subsidiaries against 55 companies and 24 individuals. Meanwhile, the Financial Secretary of Hong Kong has ordered investigations into eight major private companies in the OTB empire. The problem at OTB also spilled over to its 62 pct subsidiary - The Hongkong Industrial and Commercial Bank. In fact, OTB was just about to close a deal with Hong Leong Company to sell its stake in HICB for about HK$257 million. Not surprisingly, Hong Leong Company promptly withdrew its bid and it was later discovered that Hongkong Industrial and Commercial Bank was involved in the fraudulence. A substantial sum of HICB's non-performing loans, believed to be between HK$300 million and HK$400 million, are pledged by OTB shares that were declared valueless on the date of the Government takeover.

The impact of OTB issue was much bigger than that of Hang Lung Bank since it is one of the biggest local bank groups. Quite a number of small local banks were under pressure and found their deposits falling. The hardest hit victims was Ka Wah Bank, a small local bank with assets totaled HK$5.4 billion as at Dec. 31, 1984. In an unprecedented move, Hongkong and Shanghai Banking Corporation and Bank of China, Hong Kong, after consultation with the Government, jointly pledged to support Ka Wah Bank by extending a secured line of credit to them. While Hong Kong Bank has helped the Government in past financial crises, this was the first time that Bank of China steps in on Hong Kong's crisis. This move suggested that China is willing to play a more important role in Hong Kong even before it is due to take over from Britain.

The collapse of Hang Lung Bank and OTB has exposed the weak banking supervision in Hong Kong. Even the most ardent free-marketeers are convinced that tighter controls are necessary. Actually, the Government has started to review the banking supervision since Hang Lung's event. A team of Bank of England officials were invited to Hong Kong and they completed a confidential report on various aspects of prudent regulation in Hong Kong in March 1984. In Feb. 1985, it was officially announced that the supervision of banks and deposit-taking companies (DTCs) 9n Hong Kong would be revised and beginning in March, a number of discussion papers prepared by the Banking Commissioner's office were circulated to leading banks and DTCs. Subsequently, another revised paper summarizing the reform proposals was circulated to selected banks and DTCs. After almost one-year preparation, the proposed amendment to the Banking Ordinance, The Banking Bill 1986, was finally published in Government Gazette on march 7, 1986.

Purpose of the Study

Hong Kong is not the only place experiencing a financial panic of one form or another. Recent events, such as the Continental Illinois and Johnson Matthey affairs, have shown that even in the U.S. and Britain, where central banking are well established, the financial centre is not free of occassional shocks. The rapid financial and technological innovation, while no doubt creating new opportunities and benefits, has also enhanced the risks of financial business. Consequently, banking supervision becomes more essential and difficult job to the government.

Although the failures of some mismanaged banks and DTCs have given it a bad name, Hong Kong's financial system is still basically sound and resilient. While criticizing that the Banking Commissioner has been too lax in the past, some bankers remind that the authority should avoid the mistake of jeopardizing Hong Kong's liberal business and regulatory environment which contributes greatly to the rise of Hong Kong as an international financial centre in the past decade. Nothing can do more damage to Hong Kong's position as the third largest financial centre in the world (at least on the criterion of quite a number of foreign institutions) than a mass exodus of foreign financial institutions at a time when Tokyo is opening up its financial markets, and Singapore is still competing fiercely with Hong Kong.

The Financial Secretary of Hong Kong, Sir John Bremridge, said in his budget speech in February 1985, "The Government is not advocating regulation for regulation's sake. Our aim is to promote sound business practice, to provide a measure of protection for depositors and investors, and hence, to consolidate Hong Kong's reputation as a major financial centre."

The purpose of our report is to study the various aspects of the banking reform proposed and to see whether they are valid and justified. It is also our intention to see whether the objectives of the reform as mentioned by the Financial Secretary above will be met. In the course of the analysis, the report will also highlight the applications and impacts of the proposed changes to banks and DTCs in Hong Kong.

Scope and Limitations

Due to limitation of time and resources, our discussion will be confined to the issues contained in the Banking Bill 1986.

Specifically, our discussion will focus on the following issues:

1. Liquidity Requirement.
2. Capital Adequacy - Capital to Risk Assets Ratio (Risk Assets Ratio).
3. Discretionary Power of the Banking Commissioner.
4. Restrictions on Lending.
5. The Role of Auditors.

CHAPTER II

METHODOLOGY

In this research report, we try to touch on the up-coming banking reform in Hong Kong which has attracted public attention over the past few months. Since the reform will affect different categories of people in the community, we have to make a complete study of the past and present banking environment and draw opinions from the related groups with a view to depicting a clear picture of the reform, so that actions can be taken to reinforce and promote the energetic and prosperous financial centre of Hong Kong.

Our study will relate to some significant events on banks happened in the past few years in order to sort out the loopholes, flaws and insufficiencies in the Ordinance, and to indicate the area that has been the stumbling block to developing a sound and efficient banking system in Hong Kong. Knowing the underlying issues in the past will then lead us to project into the future direction of the path, incorporating of course the recent developments in the local community as well as overseas.

We purport to solicit comments and opinions from the widest spectrum of related personnel possible for grossing up the considerations that have to be taken in arriving at a new ordinance which is theoretically and practically sound. The related groups of personnel include:

1) Policy-making senior executives of banks representing:

   a) Foreign banks.

   b) Local banks.

   c) PRC banks.

2) Practising bank internal accountants/auditors.

3) Practising CPAs having experience in bank auditing.

The means of obtaining information include:

1) Interviewing.

2) Extracts from magazines and professional journals.

We have interviewed senior executives of banks from different countries. On the whole, their response was positive and much fruitful information has been obtained. As to publicity, most of them did not object to having their names disclosed in this report. However, with very few exceptions, those executives from the Bank of China group in Hong Kong declined any publicity. With regard to this aspect, we have decided not to disclose any names of the executives we have interviewed except that their opinion and comments are classified by country background of the banks with which these executives work for.

Conclusions drawn from the replies of the respondents will be sorted out and categorized into functional areas. Our own opinion will also be spelt out in order to arrive at an overall proposal to the amended Ordinance which we believe would provide insight to the reform.

CHAPTER III

ANTECEDENTS OF THE BANKING REFORM -- BANK FAILURES DURING 1982-1986

Bank Failures Since 1982

The Hang Lung Event

In September 1983, the Legislative Council, in an unprecedented move, passed the Hang Lung Bank (Acquisition) Bill, authorizing the Government to take over Hang Lung Bank. Due to liquidity problem, Hang Lung first experienced a run in 1982. It was at a time when the British and Chinese Governments were holding talks about the future of Hong Kong after 1997 when Hong Kong will be turned over to China. The panic from the local community, brought about by the uncertain political atmosphere, sent US$ sky high against HK$ as the public was scrambling for foreign currency. The stock and property market went down, as most people were trying to take refuge overseas, and, like a chain reaction, affected many business adversely.

The take-over was an unusual move on the part of the Government in light of its normal non-intervention policy. It was felt, however, that the main reason for its action was because of the Sino-British Agreement. Under this agreement, the Hong Kong Government has the responsibility to maintain the prosperity and stability of Hong Kong for the transitional years before 1997.

Following the bank run, several banks including some overseas banks, withdrew the facilities they previously granted Hang Lung. It subsequently led to the incapability of Hang Lung to honour cheques amounting HK$140 million and it was at this time the Government stepped in. Later, in the High Court, it was revealed that a massive cheque-kitting exercise involving US$21.7 billion was the single material factor which led to the collapse of Hang Lung Bank and Dollar Credit Finance.

Soon after the Hang Lung incident, a Special Committee consisting of economists and bankers was set up to study the case. Recommendations of the study group were that there should be government intervention for commercial failures, stronger government supervision over the banking sector, and the possibility of introducing deposit insurance.

No doubt the Hang Lung incident proved how political factors could affect monetary decisions. The run came at a time when uncertainty of the future caused panic in the local community and the Government, anxious to maintain stability in the local economy, stepped in to support the failing bank.

The OTB Event

As the Hang Lung incident gradually faded from the public's memory, in June 1985, much to the surprise of everyone, the directors of Overseas Trust Bank (hereafter called OTB) submitted a declaration to the Banking Commissioner stating that the bank was insolvent and that it was unable to continue operation. In the evening, the Financial Secretary, Sir John Bremridge, together with the Banking Commissioner, Mr. Robert Fell, ordered temporary closure of all branches of OTB until further notice. At the same time, the managing director of OTB, a Malaysian Chinese, was detained at the airport as he was trying to leave Hong Kong, carrying with him cash and securities exceeding HK$1 million. The Commercial Crimes Bureau also stepped in investigating the affairs of the bank and subsequently three other directors were also detained.

On the next day, the Legislative Council passed the Overseas Trust Bank (Acquisition) Bill authorizing the Government to take over OTB. This was the second time in three years that the Government had "nationalized" a private enterprise for preventing it from going bankrupt. Initially the cost for rescuing OTB was estimated in the region of HK$2 billion. The money was to come from the Exchange Fund which is equivalent to Hong Kong's foreign exchange reserve.

OTB has a larger asset base compared with Hang Lung and is one of the largest local banks operating in Hong Kong. It has 43 local and 8 overseas branches. The collapse of OTB was, of course, viewed as another example of weak banking supervision, of insider transaction between a bank and its shareholders.

Depositors' interests were safeguarded by government intervention but at the expenses of taxpayers. No reason was given by the Government for the sudden collapse of the bank except for suspected fraud. OTB, like Hang Lung, was also involved in the cheque-kitting cycle at some stage. Later, several former shareholders and senior executives of the bank were being charged for conspiracy to defraud shareholders and creditors of the bank.

The problems at OTB spilled over to Hong Kong Industrial and Commercial Bank (HICB), its 62%-owned subsidiary. Actually at this time, OTB was negotiating with Hong Leong Co. for the sale to the latter of OTB's 62% share of HICB for HK$256.75 million. This deal, however, finally fell with Hong Leong withdrawing its purchase agreement. On the date of government takeover, a substantial sum of HICB's non-performing loans, between HK$300 million to HK$400 million, were declared valueless and, as a result, a HK$408 million rescue package was announced to prop up the insolvent HICB.

After an initial review of OTB books, it was found that as much as HK$2 billion missing funds were loaned to companies controlled by its former directors. These transactions took place not only in Hong Kong but via OTB offshore branches, mainly in Macau and Colombo. Part of the missing funds, estimated at around HK$800 million, was lent to a finance company, Dominion Finance Ltd. headed by Simon Yip, by means of cheque-kitting exercise. The loans were approved with inadequate or no securities or collateral. As a result, a total of 87 writs claiming repayment for almost HK$1.2 billion was filled by OTB and its subsidiaries against 55 companies and 24 individuals. The sum claimed on each writ was below HK$100 million and thus none was an incident of violation of the legal lending restriction to a single borrower as laid down in the Banking Ordinance. Total exposure, however, of all these companies represented 80% of total shareholders' funds plus retained earnings of the OTB group.

The boards of OTB and HICB then petitioned the High Court to wind up 18 companies, some of which were believed to be those controlled by the ruling family. These companies were connected closely with one another with several OTB shareholders being the ultimate controllers. Following the collapse of OTB, most of the directors of these companies also resigned from their respective boards.

In order to restore the capital base of OTB, which was wiped out by a consolidated loss of $3.05 billion in the year ending June 30, 1985, the Government had to inject $2 billion to restore it. The capital injection, which was made in the form on non-interest bearing redeemable preference shares of $1 each subscribed by the Government, restored OTB's shareholders' funds to $545 million from a deficit of $1.45 billion. Aside from the $2 billion which is visible on the balance sheet, additional funds had to be injected into the bank's inner reserve. Only at this time the bank could finally operate viably again.

The additional capital acted as a cushion against continuing loses until such time as the bank could recover the debts or dispose the securities. Most of the bad debts, estimated to be as much as HK$2 billion, were from loans to parties associated with former directors and shareholders of OTB. A substantial portion of the problem loans were advanced through the bank's Macau branch which was believed to the major vehicle used to channel the missing funds.

As in the case of Hang Lung, a substantial number of depositors and banks withdrew their deposits and credit lines even after the government take-over. Cash on hand and deposits with other banks and deposit-taking companies dropped by as much as 71%. Values of certain loans had to be written down and mostly all the other accounts on the balance sheet i.e. deposits, other provisions, fixed assets etc. had to be revaluated down. As a result, the size of the balance sheet on the whole shrunk by almost

40%. The loss incurred completely wiped out shareholders' funds.

The main task for OTB's new management was to control the losses and set out procedures for recovering the doubtful loans. Also, proper internal control systems had to be set up in order to build new business.

The OTB crisis was a hard lesson for the regulatory authorities. It showed how existing banking laws failed to monitor, on a consolidated basis, excessive exposure to companies controlled by the same group of owners. But most importantly, it showed how weak the Banking Commissioner and the auditors were in detecting irregularities which apparently had existed over a long period of time. As government investigators dug deeper, their estimates of allegedly improper loans rose. Many of these loans were made to several of the bank's former executives and their associated companies. These loans were inadequately secured or backed by properties and shares whose prices have plummeted. There was a substantial portion of non-productive loans and it would take a long time before the bank could be profitable again.

The bank's problems were compounded by the difficulty it faced in trying to attract depositors. In the six months following the take-over, existing depositors defected and total customer depositors reduced by 70%. Again, this raised further questions at the Government's weak supervision of banks.

The Ka Wah Event

The OTB crisis sent a series of shock waves through the local banking circle. It affected especially the small local banks which are traditionally run by one family. As depositors lost faith, a dozen or so of these banks were subjected to widespread speculation and the Ka Wah Bank was the first to get hit. Ka Wah, controlled by a Singaporean family, had minor business association with OTB. It is a relatively small bank with only 27 local offices and one branch each in Los Angeles and New York. In order to ease the situation, in an unprecedented move, the Hong Kong Bank and the Bank of China agreed to jointly support Ka Wah. The pledge of support, made in consultation with the Government, represented a growing role in Hong Kong affairs for China before 1997.

The Bank of China, whose branch here heads a group of 13 Beijing-controlled banks, has not played such a role prior to the Ka Wah incident. The two big banks jointly extended a substantial line of credit to Ka Wah aiming at assuring depositors. Even so, due to the significant amount of non-performing loans extended to the collapsed Pan-Electric Group in Singapore, most of Ka Wah's reserves has been wiped off. In an action to safeguard the local banking system, the Hong Kong Government started nogotiating with China International Trust and Investment Corporation for the acquisition of 92% of Ka Wah's shares with a guarantee from the Hong Kong Government for the doubtful loans.

The Wing On Event

Most of the other local banks looked for stronger partners. In December 1985, Wing On Bank, which was traditionally controlled by the Kwok family, agreed to sell 51% of its shares to Hang Seng Bank. This meant, the Hong Kong and Shanghai Banking Corporation, the parent bank of Hang Seng Bank, is embracing another local bank into the group. In principle, Hang Seng will acquire a controlling interest in Wing On Bank. It was not an attractive deal for Hang Seng at the time if purely viewed from commercial viewpoint, but it is considered imperative for maintaining stability in the local banking system. This responsibility which traditionally was shouldered by Hong Kong Bank is now also shared by the Bank of China group. The transaction, of course, could be viewed as another rescue operation for a small local bank.

Apart from the unfavourable market conditions, Wing On Bank was in a tight capital position after providing for substantial bad and doubtful debts. Shareholders' funds shrunk by more than 42% compared with previous years' figures. Moreover, the bank needs stronger management.

Partnership with a strong partner should be helpful for long-term development as well as for solving immediate problems. Wing On Bank, with 50 years' history, had a strong retail customer base among the Chinese community.

The Union Bank Event

On March 27, 1986, the Government rescued another troubled local bank, Union Bank of Hong Kong. In an unprecedented move, the Banking Commissioner announced that after consultation with the Financial Secretary, he decided to take over the managerial control of Union Bank. Jardine Fleming Company, a local merchant bank, was appointed to run the bank on behalf of the Commissioner. It was also announced that the Exchange Fund had also made available a substantial credit line to the bank to meet the claims of all depositors and other creditors.

This was the first time the Banking Commissioner exercised his power under Section 13 (1) (iii) of the Banking Ordiance to take over the managerial control of a bank. But unlike the cases of Hang Lung and OTB, the Government emphasised that Union Bank is still solvent despite its liquidity and loan problems. The Commissioner explained that his action was triggered off by the prolonged absence of Union Bank's chairman Mr. Oen Yin-choy from Hong Kong since last September and the resignation of six directors, leaving the bank in a deteriorating liquidity position and without management direction.

Union Bank is a relatively small bank controlled by Southeast Asian Chinese. It is a heavy lender to many Indonesian companies which have been hit hard by falling oil prices and Indonesia's economic slowdown. Consequently, Union Bank's problem debts mounted. Furthermore, the bank's liquidity has been squeezed by a flight of deposits following rumors that the bank was in trouble since early this year.

The Union Bank event is expected to hasten the search among the remaining family-owned banks for a strong partner or the so-called "big daddy".

Despite repeated official reassurances, confidence in Hong Kong's banking system remained shaky. After the OTB take-over, officials warned that the Government might not again use public funds for another rescue. These remarks taken by the public as warning that they could expect no more government protection, prompted some depositors to defect from small local banks. Hong Kong really does not have any clearly stated government policy on shoring up banks in the event of a liquidity crunch. Without deposit insurance or a central bank to act as a lender of last resort, depositors really have no assurance of protection. The few incidents as illustrated above only affected a few relatively small local banks but still the collapse of even one or two of them could have severe repercussions.

Causes of Bank Failures

The failure of these four banks has drawn public attention to the common features of these banks. People believe that the occurance of these events do have much to do with the background of the banks.

Invariably the events happened with the local Chinese banks which established a few decades ago by the big families then in Hong Kong. At that time, banking business in Hong Kong was still at a rather stagnant stage. Competition was not keen. The banks were set up to serve mainly the local Chinese businessmen who were doing business in a traditionally conservative manner. These banks grew with the progress of the economy of Hong Kong. As Hong Kong became more internationalized, foreign banks started penetrating into this lucrative market. The foreign banks were much larger in size and used modern management concepts. Noting that the owners and the management of the Chinese banks were not well educated and that they ran the bank in the same way as they ran their other family business, they began to be driven out of the business. What they still maintained were the business relationship with the medium to small Chinese firms.

A very common feature among these Chinese banks is the management philosophy. It was commonly highly centralized in the hands of the owners of their offsprings.

A bank is different from a firm in that it uses public's money for operation. However, the centralization of power has rendered the chief executive of these Chinese banks negligent of this fact. They tended to view the bank as one of the firms they were controlling. As such they were actually taking the public depositors on a ride.

The effect of mismanagement had rendered tons of money channeled to incompetent borrowers, many of which were controlled by the directors or shareholders of the bank.

The mix-up of public and private interests had led to the subsequent failures. Many of these borrowers actually lacked the required collaterals to secure the bank loans accorded to them. Yet, tactful arrangement of diversified borrowers had made the lendings in compliance with the Banking Ordinance on credit limit.

OTB and Ka Wah were closely related to Southeast Asian Chinese businessmen. The chain of business failures among the overseas Chinese to whom these two banks had extended substantial credit was an important factor to the failure of these two banks.

These banks all have loose credit control policy. And regardless of whether there were acts of fraud, it is obvious that credits had been extended either to incompetent borrowers or to borrowers without sufficient collateral.

Consequence of Bank Failures

The series of events cautioned the public as to the capabilities of the independent auditors and the effectiveness of government supervision.

People just could not imagine how the auditors could have overlooked the seemingly apparent irregularities on the books.

The Banking Commissioner was being particularly criticized. Public complaint tended to divulge to the fact that government supervision on the banks had been too loose and imprudent. What was most sarcastical was the Banking Commissioner's comments on some of these ailing banks as "healthy" before the failures were disclosed.

As a result of these events, public opinion was diverted to a complete reform on the existing Banking Ordinance and the discretionary authority of the Banking Commissioner.

CHAPTER IV

THE 1986 PROPOSED AMENDMENTS TO THE BANKING ORDINANCE

The Existing Legislation

The following are the major areas on which the Government imposes control on the banking sector via the Banking Ordinance:

a. Maintenance of a minimum liquid asset ratio of 25%;

b. No company incorporated in Hong Kong shall be granted a banking licence unless its issued and paid-up capital is not less than $100 million;

c. Adequate provision for bad and doubtful loans should have been made against earnings;

d. No dividend should be paid unless all intangible assets have been written off and the paid-up capital and reserves should be not less than $200 million after payment of dividend;

e. No loan could be granted against the shares of the bank as collateral;

f. Loans to one individual or corporation should not exceed 25% of the paid-up capital and reserves;

g. Loans to directors of the bank and their relatives should not exceed 10% of the paid-up capita and reserves;

h. Clean loans to employees should not exceed one year salary of the employee;

i. Cannot participate in wholesale, retail, import and export trade;

j. Submit Wednesday and monthly returns reflecting the bank's financial position.

Spirit of the Ordinance

The basic spirit of the Ordinance could be summed up as follows:

1. To ensure adequate liquidity;
2. To ensure a healthy capital level;
3. To ensure any bad loans will be reflected in the earnings;
4. To safeguard the assets of the bank from "putting all eggs in one basket;"
5. To prevent overlending to bank staff;
6. To ensure the bank not going into non-bank businesses;
7. To prevent the bank from going into highly risky business where large amount of capital would be tied up;
8. To ensure the Commissioner has adequate information of the bank.

The Banking Bill 1986

The Banking Bill 1986 is a combination of existing Banking Ordinance (Cap. 155) and Deposit-taking Companies Ordinance (Cap. 328) with amendments and modifications.

While the Capital to Risk Assets Ratio is completely new, major changes concentrate on the following areas: Liquidity Ratio, Restriction on Loans, Management and Ownership, Roles of the Banking Commissioner and Audits.

We will discuss the above areas one by one, except that the Roles of the Banking Commissioner and Management and Ownership will be discussed together under the section "Discretionary Power of the Banking Commissioner".

When the Bill will come into operation is still not yet fixed, but there is a power at clause 1(2) of the Bill to appoint different dates for different provisions. It is expected that there will probably be a two-year transitional period for implementation of the Capital to Risk Assets after other provisions of the Bill are brought into operation[1] while liquidity ratio will be implemented at the time the Bill comes into operation.[2]

Liquidity Requirements

A. Specified Liquid Assets

At present, Banks and DTCs are required to maintain a minimum holding of Specified Liquid Assets which should be not less than a certain percentage of their deposit liabilities specified by the Banking Commissioner.

Specified Liquid Assets refer to the following:[3]

(a) notes and coins which are legal tender in Hong Kong or in other currency which is freely remittable to the bank in Hong Kong (bank hereinafter also refer to DTC);

(b) refined gold in the form of coin or bars situated either in Hong Kong or some other place from which the gold, or money

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[1]Banking Bill 1986, p. c207.

[2]Ibid.

[3]Banking Ordinance, Revised Edition 1983, Section 18.

into which it can be converted, is freely remittable to the bank in Hong Kong;

(c) the total balance of money payable on demand at, and money at call with, other banks or any DTC in Hong Kong or outside Hong Kong which are freely remittable to the bank in Hong Kong and held in a form approved by the Banking Commissioner;

(d) Certificates of deposit which are issued outside Hong Kong by any bank approved by the Commissioner in any foreign currency freely remittable to the bank in Hong Kong and marketable in a manner satisfactory to the Commissioner. In normal practice, those certificates of deposit issued by banks in international financial centres like London, New York, Singapore, and Tokyo are acceptable to the Commissioner to be treated as liquid assets.

(e) such money market instruments, whether totally or to such limited extent, as the Financial Secretary may specify by notice in Gazette;

(f) treasury bills, maturing within 93 days, issued by the Government or by the U.K. Government or Government of any other country specified by the Financial Secretary;

(g) money at short notice at other banks or DTCs in Hong Kong or at any bank outside Hong Kong, which is freely remittable to the bank in Hong Kong and held in a form approved by the Commissioner;

(h) such money market instruments, either totally or to such limited extent, other than those specified under item (e) above, as the Financial Secretary may specify by notice in the Gazette;

(i) bills of exchange payable at usance outside Hong Kong and discountable in a currency which is freely remittable to the bank in Hong Kong;

(j) bills of exchange payable after sight outside Hong Kong in a currency freely remittable to the bank in Hong Kong

(k) such securities, other than those specified in the next item, issued or guaranteed by the Government, or the Government of any other country, as may be specified by the Financial Secretary and published in the Gazette;

(l) securities with less than 5 years to maturity issued or guaranteed by the Government or the Government of the United Kingdom, if -

i) they are quoted on a Stock Exchange in London, Hong Kong or New York;

ii) they have been dealt in during the preceeding 6 months;

iii) payment of interest thereon is not in arrear.

In item (c), the term "Money at Call" means money payable within not more than 24 hours of a demand, excluding money payable on demand. Interbank deposits maturing the next day and overnight interbank deposits are also classified as Money at Call.

In item (g), the term "Money at Short Notice" means money, other than Money at Call and Money Payable on Demand, payable within 7 days of a demand therefore. Interbank deposits maturing within 7 days, excluding those maturing the next day, and interbank 1-week deposits are also classified as Money at Short Notice.

However, when a bank/DTC is claiming its balance of money payable on demand, money at call and money at short notice as specified liquid assets, its total liabilities in respect of those

3 items owing to other banks or DTCs should be deducted accordingly.

B. Present Liquidity Requirement

In accordance with the Banking Ordinance, a bank has to maintain a minimum holding of Specified Liquid Assets not less than 25% of the deposit liabilities of the bank during each month. In addition, the Specified Liquid Assets held shall include not less than the equivalent of 15% of the deposit liabilities of the bank in the form of item (a), (b), (c), (d), (e) and (f) as listed above.

i)	Specified Liquid Assets (a) + (b) + (c).....+(f)	=	Not less than 15% of total Deposit Liabilities
ii)	Specified Liquid Assets (a) + (b) + (c).....+(l)	=	Not less than 25% of total Deposit Liabilities

The Deposit Liabilities of a bank/DTC refer to its gross demand, time and savings account liabilities, excluding amounts owing to otherbanks or any deposit-taking company. The arithmatic means of a bank's specified liquid assets and deposit liabilities on each Wednesday, or the last preceding working day when Wednesday is a public holiday, is calculated and is regarded as the liquidity ratio maintained by the bank for that particular month. Reports of liquidity ratio on each Wednesday and the arithmatic mean for each month are submitted to the Banking Commissioner for inspection.

As for deposit-taking compnies, the requirement is slightly different though definition of Specified Liquid Assets and method of calculating interbank assets are identical.

In the case of deposit-taking companies, Deposit Liabilities are classified into two categories:

DL(A) -- Deposit liabilities repayable within 7 days

DL(B) -- Deposit liabilities repayable after 7 days

The following requirements have to be fulfilled.

(i) The total amount of Specified Liquid Assets in the form of Item (a) to (f) as listed above	=	Not less than 60% of (30% DL(a) + 15% DL(b))
(ii) The aggregate amount of Specified Liquid Assets in the form of Item (a) to (l)	=	Not less than 30% DL(A) + 15% DL(B)

C. Present Loopholes

As mentioned above, a bank's/DTC's borrowing from other banks or deposit-taking companies in Hong Kong within 7 days have to be deducted from its total balance of money payable on demand, at call and at short notice accordingly. However, those borrowings from banks outside Hong Kong are not accountable for the reduction. Taking advantage of this, a bank can creat as many artificial specified liquid assets as it wishes, using the technique of round-tripping via offshore bank intermediaries.

For example, a bank can create US$100 million Specified Liquid Assets on Wednesday by the following transactions:

(i) Borrow from its London branch US$100 million repayable that next day

(ii) Value the same day, lend to its Singapore branch US$100 million repayable the next day

(iii) Its Singapore branch lend back the US$L00 million to its London branch for the same tenor

No movement of funds is necessary out of the above transactions.

Since the borrowing from its London branch is not to be reduced from its interbank assets based on the ground that the lender is outside Hong Kong, the bank has increased its total balance of Money at Call by US$100 million, equivalent to HK$780 million, and thereby fulfill the liquidity requirement.

Lending overnight money in domestic interbank market in foreign currencies and squaring its position by borrowing back from other banks outside Hong Kong will have the same effect, but it may cost the bank more expenses such as brokerage and telex chargs since it involves real interbank transactions and movement of funds. We were told by more than one international money brokers that every Wednesday quite a number of banks often refuse to borrow overnight deposits from local lender except those in Hong Kong dollars which is impossible to borrow from sources outside Hong Kong. As the size of the Euro-currency market is so big that it is easy for a bank to borrow substantial amount of currency like U.S. dollar, banks can easily create artificial specified liquid assets as they wish.

It seems that the "Roundtripping" is an open secret in the banking industry. We have chosen a very small sample of 15 money market dealers of Treasury Departments from various banks and deposit-taking companies. More than half of them admitted that their institutions had used the roundtripping when their holding of specified liquid assets were below the required percentage. Some were done through real transactions with various counterparties while others were done just over the books of their own overseas branches.

Although our sample size is certainly too small, it at least proved that roundtrippig does exist and is used by some institutions from time to time.

D. New Liquidity Ratio Requirement

In view of the above loophole, a new liquidity ratio requirement is proposed in the Banking Bill 1986. It is in fact a different approach to measure the liquidity of a bank or deposit-taking company.

The liquidity ratio of a bank or DTC (hereinafter called an authorized institution) shall be calculated as a ratio between the Liquefiable Assets and Qualifying Liabilities. And it shall be calculated for each month on the basis of the average of the daily liquidity ratio for that month.[1]

It is proposed that both banks and DTCs should maintain a liquidity ratio of not less than 25% in any calendar month, although the percentage may be varied by the Financial Secretary by notice in the Gazette if he thinks it fit to do so.

The Qualifying Liabilities of an authorized institution is defined as the sum of :

i) its net interbank liabilities (including marketable claims) both in and outside Hong Kong; and

ii) all its other liabilities

maturing or callable within one month.[2]

The Liquefiable Assets of an authorized institution shall be calculated by adding the book value or current market value,

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[1] Banking Bill 1986, Part XVIII.

[2] Ibid., Fourth Schedule.

whichever is the lesser, in Hong Kong dollars, of such of its following assets which are freely available to meet any qualifying liabilities:

(a) net interbank claims (including marketable claims) both in and outside Hong Kong maturing or callable within one month;

(b) cash in till;

(c) gold;

(d) unmatured discountable export bills maturing within 6 months and export bills which are payable after sight, denominated in a currency freely convertible into Hong Kong dollars;

(e) bills, certificates, notes, paper and debt securities (other than marketable claims maturing or callable within one month) which:

  (i) are negotiable;

  (ii) have a remaining term to maturity of not more than 10 years;

  (iii) are issued by persons whose debts have not been in arrears within the immediatey preceeding five years;

  (iv) are denominated and traded in a currency freely convertible into Hong Kong dollars; and

  (v) are quoted on a stock exchange approved by the Commissioner for the purpose of this Schedule or by not less than 2 brokers recognized by the Commissioner;

(f) securities issued or guaranteed by the Government or any other Government approved by the Commissioner;

(g) performing loans, instalments of loans including interest on such loans which will be paid in cash within one month, but excluding overdrafts and other loans repayable at short notice.[1]

The new Liquidity Ratio Requirement will replace the Specified Liquid Assets requirement under the existing legislation. If we compare the Liquefiable Assets with the Specified Liquid Assets, we will find that they are more or less the same. Item (g), performing loans repayable within one month, is newly added. The requirements and the range of securities to be included as liquid assets are more specific than the existing statutes. It appears that the Commissioner intends to allow more variety of securities such as Euro-notes and commercial papers to be treated as liquefiable assets.

The method of calculating the new ratio, together with the assets and liabilities to be taken into account, are contained in the Schedule to the Bill so that it will be much easier for the Commissioner to make any alteration when it is deemed necessary.

In the explanatory memorandum of the Bill, it is said that the ratio is considered to be an improvement over existing liquidity requirements because those requirements take no account of cash inflows and outflows an institution reasonably expects over a period of time. In fact, the roundtripping will no longer be workable since borrowing from banks outside Hong Kong will also be counted under the new method of calculation.

Nevertheless some people argue that a bank can still circumvent the new requirement by "borrowing long and lending short". For instance, if a bank borrow HK$100 million for two months and lend back the same amount for a period of one month, the

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[1]Banking Bill 1986, Fourth Schedule.

bank will have an extra liquefiable assets for HK$100 million.

It is true that a bank can create liquefiable assets by using above method; but by so doing, the bank has created a maturity gap which is subject to fluctuation of interest rate and the cost for the bank may be high as normally short-term money is cheaper than long term. Besides, it will be more easily discoveraged by the Commissioner if both transactions are done through the books of the bank's overseas branches and interest rates are artifically fixed at the same price.

Some bankers believed that the new liquidity ratio will make banks and DTCs less aggressive in mismatching their borrowing and lending.[1] AS the calculation format is more strict, some institutions will need to modify their policies on treasury management. It is now a common practice for banks to adopt a "Borrowing short and lending long" policy, i.e. to borrow short-term money to finance longer term loans as short term funds are cheaper given a normal positive-slope yield curve. The new requirement will still allow banks/DTCs to mismatch their borrowing and lending, but the maturity gap between short-term funds and long-term loans will be narrowed, since an institution will have to match at least its assets and liabilities within the short end.

Mr. K. K. Wong, the Assistant Banking Commissioner, said that it is not desirable for an institution to be too aggressive in its mismatch of funding and that the maturity gap will be closely monitored in future through the new monethly statistical return.[2]

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[1]Cecilia Ko, "Making Banks less Aggressive", South China Morning Post, March 17, 1986.

[2]Ibid.

It should also be noted that a contravention of the new liquidity ratio will not be an offence in itself, but failure to report the contravention or to carry out remedial action required by the Commissioner is an offence. An authorized institution may appeal to the Financial Secretary against any such remedial action. The Commissioner also has the power to vary the ratio for particular authorized institutions but, unlike thecapital to risk assets ratio to be discussed later, no upper limit is set. This provides the Commissioner with flexibility to cope with situations where some smaller local banks are hurt by rumor and find themselves unable to borrow money from the interbank market while depositors are withdrawing huge amount of money from them. And should the Commissioner foresees that a certain institution may run into troubles and have difficulty in funding, he may request the bank to keep a higher liquidity ratio beforehand.

E. Charges over Bank's Assets

Apart from the new liquidity ratio requirement, a new clause, Clause 110, has been inserted in Part XVIII - LIQUIDITY RATIO OF AUTHORIZED INSTITUTIONS AND MATTERS AFFECTING LIQUIDITY RATIO of the Bill. Although it does not directly relate to the liquidity ratio, it relates to matters which may affect the ratio.

The clause provides that an authorized institution shall not, except with the approval of the Commissioner, cause the sum of all charges over its assets in Hong Kong to exceed 5% of the aggregate total of the value of those assets. And when any civil proceedings has been instituted against the authorized institution to recover claimed indebtedness, the institution shall, if the proceeding could adversely affect the financial position of the institution, notify the Commissioner of the proceeding.

The term "charges" here includes liens, encumbrances, equitable interests and third party rights.[1]

Capital Adequacy and Capital
to Risk Assets Ratio

Capital Adequacy is important to the banking system since one of the primary functions of capital is to enable losses to be sustained without threatening the closure of bank or otherwise prejudicing the interests of depositors.

The existing legislation prescribes minimum capital requirements for banks and deposit-taking companies:

Licensed Banks:	Issued and Paid-up Share Caspital	Not less than HK$100,000,000
Licensed DTCs:	Issued Share Capital	Not less than HK$100,000,000
	Paid-up Share Capital	Not less than HK$ 75,000,000
Registered DTCs:	Paid-up Share Capital	Not less than HK$ 10,000,000

Since the minimum capital requirements for banks and deposit-taking companies bear no relationship to the amount and riskiness of the assets they support, a measure of capital to risk assets ratio is introduced to remedy the deficiency. The ratio simply compares capital with risk assets as a common measure of capital adequacy. Originally, the ratio was proposed to be set at 10%. Due to objections from a large number of banks and DTCs, it has finally been set at 5%. However, the Commissioner has the power to increase the rtio for particular institutions to a

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[1]Banking Bill 1986, Clause 110 (6).

"ceiling" of 8% in the case of banks and 10% in the case of deposit-taking companies, though that particular bank or DTC may appeal to the Financial Secretary against the imposition of such higher ratio.

The method of calculation of the ratio, together with the capital base and the risk assets to be taken into account, are contained in the Third Schedule to the Bill so that it may be easier for the Commissioner to make any alteration when it is deemed necessary.

A. Capital Base

According to the Schedule, the capital base of a bank/DTC shall be calculated by adding up the value of the following:

(a) paid-up capital;

(b) perpetual subordinated debt convertible into equity at option of issuer, but excluding any amount in excess of half the paid-up capital;

(c) general reserves, including inner reserves, share premium account and revaluation reserves, but excluding provisions however described; and

(d) undistributed profits, but excluding unprovided but declared dividends not yet paid.

And by deducting the value of the following:

(i) investments in any subsidiary, any associated company and any holding company;

(ii) loans and other expenses which in the opinion of the Commissioner are of a capital nature; and

(iii) goodwill.[1]

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[1]Banking Bill 1986, Third Schedule.

B. Risk Assets

Different risk weights will be used to multiply the value of various categories of assets when computing the total value of risk assets of a certain authorized institution.

(a) Category I - risk weight 0.0:

(i) Government certificates of indebtedness held for note issue;

(ii) cash in till; and

(iii) contingent liabilities in respect of forward foreign exchange contracts, interest rate swaps, option contracts, futures contracts, bills held for collection of customers, and shipping guarantees and trust receipts in respect of unmatured trade finance transactions.

(b) Category II - risk weight 0.2:

(i) unsubordinated claims on or contingent liabilities in respect of eligible banks[1] or eligible governments,[2] or having such banks or governments unconditional guarantee, maturing or callable within less than one year;

(ii) claims or contingent liabilities secured by cash or

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[1]Eligible bank means any bank or licensed deposit-taking company in Hong Kong or any other bank incorporated outside Hong Kong except such a bank which is, in the opinion of the Commissioner, not adequately supervised by the appropriate recognized banking supervisory authority of the place in which it is incorporated.

[2]Eligible government means the Hong Kong government; any other government whose debt has not been in arrears at any time during the 5 years immediately preceding the date on which the relevant calculation of the capital to risk assets ratio is made; and any other government approved by the Commissioner.

cash deposits with the institution under its complete control; and

(iii) bullion or listed securities held against the institution's liability to customers or under resale agreements.

(c) Category III - risk weight 0.5:

(i) negotiable unsubordinated bills, notes, paper and listed securities, at current market value, with a remaining term to maturity of not less than one and not more than 10 years, drawn on or issued or guaranteed by eligible banks or eligible governments, and which are quoted on a stock exchange approved by the Commissioner or by not less than 2 brokers recognized by the Commissioner for this purpose;

(ii) unmatured import and export trade finance through bills or notes maturing within 6 months;

(iii) unsubordinated claims on or contingent liabilities in respect of registered deposit-taking companies (except deposit-taking companies the registration of which is for the time being suspended) or having such companies unconditional guarantee, maturing or callable within less than one year; and

(iv) all contingent liabilities not otherwise specified in this term, and including any net underwriting commitments.

(d) Category IV - risk weight 1.0:

All other assets.

C. Capital to Risk Assets Ratio

The ratio is to be calculated as follows:

$$\text{CAPITAL TO RISK ASSETS RATIO} = \frac{\text{CAPITAL BASE}}{\text{RISK ASSETS}}$$

The Risk Assets Ratio is one of the most controversial tropics when consultation with the banking community was being conducted by the Commissioner.

Originally, it was suggested that the ratio should be set at 10%; but due to objections from the banking community, the ratio was finally set at 5%. It was also decided that the ratio should only be applicable to those authorized institutions incorporated in Hong Kong based on the ground that it should be the sole responsibility for foreign banking authority to supervise their own banks. However, some foreign banks are still not pleased with the arrangement. Japanese banks' subsidiary DTCs are especially upset by the new ratio which they find it hard to comply. Due to Hong Kong's low taxation and relatively free regulatory environment, most of the Japanese DTCs are incorporated in Hong Kong to act on behalf of their parents to arrange and book offshore loans for the Asian region. The DTCs here are also used to issue Eurodollar bond or notes under guarantee of their parents.

It is reported that out of 23 DTCs of Japanese banks, only three comply with the statutory ratio of 5% and the ratio of the others only averages about 3%.[1] As a large portion of their asset portfolios comprises offshore loans, loans to parent banks

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[1]Cecilia Ko, "Japanese may pull out DTC Risk Assets", South China Morning Post, Mawrch 17, 1986.

and securities held as trading assets, Japanese bankers argue that all DTCs doing similiar offshore banking business like them should be exempted from the risk assets ratio measure.

Before the disclosure of the banking bill, it was reported that the present three-tier banking system might be changed and the Commissioner had considered establishing a new class of "limited service banks" to solve the problem.[1] As the Japanese Government is also considering introducing a similar capital adequacy ratio, Japanese bankers may have to accept the concept eventually although further debate on the calculation of the ratio between them and the Commissioner seems to be unavoidable.

As for local banks and DTCs, it would certainly be tough years ahead for them to adjust to the new requirement, though a two-year transitional period will be given to them.

Their capital base and asset composition will certainly have to be restructured. It is expected that smaller local banks will be put into a more difficult position to compete with foreign competitors once the Risk Assets Ratio is imposed on them.

Discretionary Power of the Banking Commissioner

One of the most important things in the proposed banking reform is the change of approach from rule-based supervision to the use of more discretionary judgement by the Banking Commissioner. Under the new legislation, the Commissioner will be granted more power to operate more on a discretionary basis, relying more on his judgements about the capacity of management in each bank/DTC to

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[1]Ming Pao Evening News, March 13, 1986.

cope with the challenges it faces.

In Clause 7 of the Banking Bill, it is stated that the principal function of the Commissioner is to promote the general stability and effective working of the banking system and the Commissioner shall:

(a) be responsible for supervising compliance with the provisions of Banking Ordinance;

(b) take all reasonable steps to ensure that the principal places of business, local branches, overseas branches and overseas representative offices of all authorised institutions and local representative offices are operated in a responsible, honest and business-like manner;

(c) promote and encourage proper standards of conduct and sound business practices amongst authorized institutions;

(d) suppress or aid in suppressing illegal, dishonourable or improper practices in relation to the business practices of authorized institutions;

(e) co-operate with and assist recognized banking supervisory authorities of any place outside Hong Kong, whenever appropriate, to the extent permitted by this or any other Ordinance; and

(f) consider and propose reforms of the law relating to banking business and the business of taking deposits.[1]

This is the first time the functions of the Commissioner is

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[1]Banking Bill 1986, Clause 7, p. C135.

clearly defined in banking statutes and it reflects the different emphases in the approach to prudential supervision -- one that relies more on the Commissioner's discretion and qualitative judgement than previously.

A. Discretionary Power

Based on the painful experience gained from Hang Lung and OTB events and in a move to prevent bank fraud and mismanagement, the Banking Commissioner will be given additional discretionary power under the Banking Bill.

At Part X of the Bill, the existing powers of the Commissioner and Governor in Council over banks are extended to deposit-taking companies. In addition, some other discretionary powers are granted to the Commissioner. For example:

(i) Approval of exercising 10% or more acquired Voting Power: Clause 70(1) of the Bill provides that, after the commencement of the Bill, any person who acquired, whether alone or in concert with others, 10% or more of the voting power at any general meeting of a bank/DTC incorporated in Hong Kong shall not exercise his voting power unless he has obtained the Commissioner's approval to do so.

(ii) Approval of Controllers exercising their Power: Clause 72(1) of the Bill provides that, after the Bill comes into operation, no controller[1] of a

[1]According to Clause 2 of Banking Bill 1986, "Controller" means any person -

(a) in accordance with whose directions or instructions the directors of the company or of another company of which it is a subsidiary (or any of them) are accustomed to act; or

(b) who is entitled to exercise, or control the exercise, of more than 50 percent of the voting power at any general meeting of the company or of another company of which it is a subsidiary.

bank/DTC shall exercise his control of the institution by giving any directions or instructions to the directors of the institution unless he has the Commissioner's approval to do so.

(iii) Approval of Appointment of Director or Secretary: Clause 72(2) provides that after the commencement of the Bill, the appointment of directors and company secretaries of a bank or DTC will be subject to consent in writing of the Commissioner.

On the whole, the ownership and management of any authorized institution incorporated in Hong Kong will be more closely monitored by the Banking Commissioner in order to reduce the risk of mismanagement or fraudulent management which have been found in recent events to be the root cause of bank failures.

As discussed in previous sections, the Commissioner will also be empowered to vary the liquidity ratio for particular authorized institutions, without upper limit, and to increase the Capital to Risk Assets Ratio for particular banks with a ceiling of not more than 8% and DTCs for not more than 10%. The device is to enrich the Commissioner with flexibility to cope with situations where he find a bank or a DTC is being run improperly.

B. <u>Safeguards and Accountability</u>

Safeguards against abuse of Commissioner's discretionary powers are provided in the Banking Bill. Banks, DTCs or other parties concerned have the right to appeal to the Financial Secretary or the Governor in Council in the above mentioned cases when the Commissioner is exercising his discretion. Also counter balancing the Commissioner's expanded role are the reporting requirements at Clause 9 of the Bill.

The Commissioner is required to produce an annual report for inspection to the Governor in Council on the working of the Banking Ordiance and the activities of his office. In the report, the Commissioner is required to draw attention to any breach or avoidance of the Ordinance that has come to his notice or any irregularity discovered by him in the accounts and records of any authorized institution which he think is important.

The report will be published, in whole or in part, subject to consent of the Governor in Council. Apart from the annual report, the Governor has the power to request a report from the Commissioner at any time.

Mr. Robert Fell, the Banking Commissioner, described the annual report as an anchor of accountability. He said that though the report cannot comment on individual banks under the nursery of the Commission, it can explain how the Commissioner had dealt with some publicised cases. And thereby the general guidelines and criteria based on which the Commissioner had exercised his discretionary powers would be shown.[1]

In order to satisfactorily implement his widened duties under the Bill, it is estimated that the Commissioner's office will require an additional 28 posts in 1986-87 and another 16 posts in 1987-88. The annual staff costs will thus be increased by $6.6 million in the first year of the Bill's operation and $10.1 million in subsequent years.[2]

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[1]Cecilia Ko, "Assurance on Banking", South China Morning Post, March 14, 1986.

[2]Banking Bill 1986, Explanatory Memorandum, p. C208.

In fact, the wide discretionary powers we discussed above have aroused great concern in the banking industry. Mr. Robert Fell, Banking Commissioner, stressed that the Bill did not give any great new accretion of powers; instead, he said, "The difference now is that the Commissioner is being urged to use his powers and a clear remit for action is being given."[1]

Even so, whether adequate safeguards have been provided in the Banking Bill is still a controversial issue.

Restrictions on Lending

To avoid concentration of risks, existing legislation prescribes limitations on total of advances, especially unsecured ones, and other "non-banking" interests such as holding of share capital of other companies and interests in lands. The Banking Bill 1986 basically leaves all these limitations unchanged.

But the definition of "company" is modified. The existing Banking Ordinance defines "company" as:

(a) incorporated under the Companies Ordinance; or

(b) incorporated by any other Ordinance; or

(c) which is incorporated outside Hong Kong and has complied with the provisions of section 333 of the Companies Ordinance.[2]

The Banking Bill 1986, when defining the word "company", keeps (a) and (b) above unchanged, but (c) was shortened to:

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[1]Cecilia Ko, "Assurance on Banking", South China Morning Post, March 14, 1986.

[2]Banking Ordinance, Part I, Section 2.

(c) incorporated outside Hong Kong.

Since Section 333 of the Companies Ordinance refers to overseas companies which establish a place of business in Hong Kong, the simplified definition in the Bill will cover any overseas company no matter it has established a place of business in Hong Kong or not. By so doing, the loophole of lending to overseas company without a place of business in Hong Kong to avoid the restriction on lending is plugged.

Furthermore, two new clauses are introduced as follows:

(i) In addition to the existing restriction that a bank/DTC shall not grant any advance, loan or credit facility against the security of its own shares, Clause 80(2) of the Bill provides that a bank/DTC shall not, except with the approval of the Commissioner, grant any advance, loan or credit facility against the security of the shares of its holding company or any subsidiary of the institution itself or its holding company.

(ii) Clause 82 of the Bill provides that the Commissioner may, after consultation with the Financial Secretary, by notice in the Gazette, issue directions applicable to all or a certain class of authorized institutions requiring them not to engage in a specific type of business practices which, in the opinion of the Commissioner, will or may cause the soundness of the financial position of authorized institutions to be dependent upon the soundness of the financial position of a single party.

The new restriction suggests that the Banking Commissioner will take a more severe approach to prevent malpractice in lending. If we take into account the losses which banks and DTCs have suffered due to the Carrian or similar events, it appears that it is justified to be so.

Audits

Past events like Hang Lung Bank and Overseas Trust Bank issues have suggested that bank's auditors should play a more important role as a third party to monitor and discover irregularities. Therefore, it is the intention of the Commissioner to strengthen the relationship of Bank's auditors and himself by establishing a form of contact that is known to and approved by the client bank.

To achieve this objective, two new clauses are contained in the Bill. Clause 61 provides that a tripartite meeting between the governing board of an authorized institution, any auditor of the institution, including any auditor who has acted for the institution for any period not earlier than 9 months ago, and the Commissioner to discuss matters relating to the institution. The meeting can be requested by any of the above parties.

Clause 62 of the Bill empowers the Commissioner to refer to the Disciplinary Committee of the Society of Accountants cases of negligence or serious misconduct by any auditor of an authorized institution.

Other audit requirements presently contained in the Banking Ordinance is basically unchanged and is extended by the Banking Bill to be applicable also to deposit-taking companies. By so doing, the Commissioner is empowered to appoint a second auditor for a deposit-taking company if it is found necessary.

CHAPTER V

BANKERS' OPINIONS ON THE PROPOSED REFORM AND ITS IMPLICATION

Opinions from banking officials of various banks and DTCs have been collected through interviews on the following aspects:

On Discretionary Power of the Commissioner

The widened power of the Banking Commissioner has aroused great concern from bankers. Clause 70 and 72 of the Bill requires that a controller has to apply for the Commissioner's approval before exercising his voting power and giving directions or instructions to the directors of the institution. A banker we interviewed criticised that this is against the non-intervention policy and free enterprise spirit which have long been adopted by the Government and is one of the major causes of the success of Hong Kong as an international financial centre. Besides, on what basis can the Commissioner decide whether a person should be approved to exercise his voting power.

The requirement that appointment of director or secretary of an authorized institution shall be subject to consent of the Commissioner is also criticised by the banker. Though it was discovered that the failures of Hang Lung Bank and OTB were due to misconduct of directors, the requirement may not be an effective measure to prevent similar events from happening again. Rather, the banker suggested, improvement of the quality of the Commissioner's supervision and audits of banks' auditors is more important.

Though safeguards have been introduced in the Banking Bill, some benkers still expressed their concern on abuse of the Commissioner's power, and above all, the quality of his staff to make efficient use of the powers.

On Liquidity Ratio

Some bankers expected that the Hong Kong capital market will benefit from the new liquidity requirement since more kinds of securities such as notes and commercial papers are included in the Bill to be treated as liquefiable assets. Banks and DTCs will certainly be encouraged by the new requirement to purchase and hold more securities in their portfolio and thereby foster the growth of the capital market.

Another banker told us that he expected there might be a change of practice in granting loan form banks. More loans will be structured and documented on a short term basis with the understanding that renewal will normally be granted upon maturity so as those loans can be treated as liquefiable assets.

Though the loophole of creating artificial "Specified Liquid Assets" by roundtripping as discussed in previous chapter can be prevented in the new requirement, a banker we interviewed pointed out that banks or DTCs can still create artifical liquefiable assets by lending to their overseas branch money with maturity of less than one month while borrowing back from the branch same amount of funds with maturity longer than one month. Although a maturity gap may be created and loss of interest may occur due to positive yield curve, it will be quite easy for the bank to get back compensation from its branch in some other way. For example, by making up two foreign exchange transactions with the same branch with the design that the bank buys low and sells high, the bank can easily earn back the loss. Of course, the banker pointed out, it could be possible for banks, especially foreign banks with several branches in various financial centres, to create artificial liquefiable assets in a more disguised way.

Another opinion from an accountant of a bank is that under the existing legislation, the liquidity ratio is calculated every Wednesday, but the Banking Bill requires that the new liquidity ratio shall be calculated daily. According to the accountant, this will increase the operation cost of a bank substantially. We were told that this opinion has been passed to the Commissioner and it is being considered whether amendment will be made.

On Risk Assets Ratio

The ratio will only be imposed on locally incorporated institutions. An official from a local bank claimed that the measurement would put local banks and DTCs into a more difficult position to compete with foreign banks. "For Japanese banks and most of the PRC banks," he said, "there is not any similiar requirement for them to follow in their home countries and they will be in a much better position to compete with us."

Another issue concerning the Risk Assets Ratio was the Risk Weight assigned to the interbank claims on registered DTCs. Originally, it was proposed that a Risk Weight of 1.0 should be assigned to claims on registered DTCs. Due to strong objection from registered DTCs, it was eventually assigned a Risk Weight of

0.5. We were told by some bankers that the Hong Kong Deposit-taking Companies Association is trying to persuade the Government to assign a Risk Weight of 0.2 to those bank-related registered DTCs. A banker we interviewed told us that if the present proposal in the Bill remained unchanged, it would be more difficult for registered DTCs to borrow money from interbank market since for claims on banks and licensed DTCs the Risk Weight is only 0.2. Eventually, registered DTCs may have to pay premium above market interest rate.

On Restrictions on Lending

Clause 82 is controversial. It provides that the Commissioner may by notice in the Gazette, issue directions to Banks/DTCs not to engage in certain business practices which the Commissioner is of the opinion that it may cause the soundness of the financial psoition of authorized institutions to be dependent upon the soundness of the financial position of a single party.

The purpose of this clause is clearly to avoid concentration of risks. However, a banker cautioned that if the Commissioner issues such kind of directions in the Gazette, the image of the banking industry as well as the single party concerned may be seriously affected. It may be especially unfair for the single party affected as it may not be able to raise funds again locally. some institutions are upset by the wording "directions" and it is said that the Commissioner is considering replacing it with term like "guidelines" in future.

On Audits

It appears that both the banking community and accounting professionals welcome the idea of triparitite meetings and the power endowed to the Commissioner to refer to the Disciplinary Committee of the Society of Accountants in case of negligence or serious misconduct by any auditor of an authorized institution. All agreed that quality of bank auditing should be improved and co-operation between banks' auditors and the Commissioner should be strengthened so as to help improving supervision on authorized institutions.

Generally speaking, it appears to us that the principles behind the proposed banking reform are accepted by the banking industry though some refinement of the Bill are suggested. All of the bankers we interviewed agreed that a stricter supervision on banks and DTCs are necessary in order to strengthen the banking and financial systems as well as enhancing Hong Kong's status as an international financial centre. In fact, more than one bankers pointed out that Hong Kong is now facing the challenge not only from Singapore but also from Tokyo as Tokyo market is now being opened and Japanese Yen is undergoing the process of internationalization. It is, therefore, crucial for Hong Kong to reform its banking industry to bring itself to a healthier condition.

With regard to other issues which have been raised and discussed but eventually excluded in the Bill, such as Deposit Insurance, establishment of discount window, lender of last resort and disclosure of banks' inner reserves, bankers' opinions seems to be quite divided. However, the suggestion to create a special category of bank, the limited service bank, seems to be welcomed by the majority. Due to limitation of time and resources, these issues will not be discussed in this report.

CHAPTER VII

COMMENTS AND RECOMMENDATIONS

The failures of banks in Hong Kong since 1983 have exposed weak banking supervision and incompetent or imprudent management of banks. The proposed banking reform is specially devised to minimize the risk of future banking failures and to strengthen the banking system as well as to enhance Hong Kong's status as an international financial centre.

We agree with the general principles behind the Bill that supervisory approach should be shifted from a purely rule-based to a more flexible and discretionary base. Nevertheless, we share the views of many bankers and are a bit worried that the widened power endowed to the Commissioner may be abused. As pointed out by some bankers, legislation is one thing and the capability of the authorities to detect irregularities and to diagnose whether a bank is in difficulty is another.

As discussed in previous chapters, some loopholes under the existing legislation have been plugged by the Banking Bill. However, some other loopholes will emerge as circumstances change. In reality, people are always wise enough to get round even the tightest rules and law enforcers are forced to play the never-ending game of plugging new loopholes. Therefore, it is more important to continue upgrading the quality of supervision rather than changing the legislation. We strongly recommend that major effort should be made to improve the quality of the Banking Commissioner office.

Based on our study of the Banking Bill and opinions collected from various bankers, we would like to elaborate our viewpoints on the following aspects:

On Capital to Risk Assets Ratio

We are of the opinion that the Capital to Risk Assets Ratio introduced in the Bill is an effective measure to restrict banks and DTCs from overlending. Although some definitions need to be further clarified, the formula for calculation suggested in Fourth Schedule of the Bill is basically acceptable.

We support the proposal of creating a new category of limited service banking for those institutions doing offshore banking business. As they are supposed to be restricted from taking deposits from the public, it is reasonable that they should be allowed to maintain a lower percentage of Risk Assets Ratio. As Hong Kong is now facing fierce competition from Tokyo, Singapore as well as Sydney as the No. 1 financial centre in Asia, we recommend that Government should seriously consider this suggestion. We estimate that at least 30 DTCs will be qualified to be classified in the new category and more foreign institutions will be lured to open their offshore banking arms here, given the low taxation in Hong Kong.

Regarding the suggestion that those bank-related registered DTCs should be assigned a Risk Weight of 0.2 instead of 0.5, we are of the opinion that as registered DTCs are smaller in size in terms of capital, and as those bank-related DTCs can easily get their funds from their parent companies, it is not necessary to assign to them a lower risk weight identical with that of licensed banks and licensed DTCs.

On Liquidity Ratio

We are of the opinion that the new liquidity requirement is basically an improvement of the existing requirement, though banks can still create artificial liquefiable assets by borrowing long while lending short, as discussed in previous chapter.

The Bill requires that the liquidity ratio shall be calculated on the basis of the average of the daily liquidity ratio. We share the view of some bankers that it may greatly increase the operation cost of authorized institutions and suggest that it should be the average of the liquidity ratio of each Wednesday as required by the existing legislation. However, the Commissioner shall be enpowered to require a particular institution to calculate the ratio daily if it is deemed necessary.

On Discretionary Power of the Commissioner

We share the view of some bankers that the Bill has given too wide discretionary power to the Commissioner. The provisions that controller shall not exercise his acquired voting power without the Commissioner's approval and that the appointment of a director or secretary of an authorized institution shall be subject to the Commissioner's consent are apparently intended to upgrade the quality of ownership and management of authorized institutions. Though past events like Hang Lung and OTB show that misconduct of management was crucial to bank failures, the provisions are not necessarily effective devices as it will be quite difficult for the Commissioner to set up an objective criterion to decide who should be approved to exercise his voting power and who should be allowed to be appointed as a director or secretary of an authorized institution. On the contrary, it may increase the workload of the Commissioner and it is against the non-intervention policy of the Government.

We recommend that both of the above provisions should be abolished.

On Restrictions on Lending

Clause 82 of the Bill provides that the Commissioner may, by notice in the Gazette, issue directions to authorized institutions not to engage in business practices which, in the opinion of the Commissioner, will or may cause the soundness of the financial position of authorized institutions to be dependent upon the soundness of the financial position of a single party. We share the views of many bankers that the provision may result in an unnecessary intervention in the development of the banking industry. We suggest that this clause should be abolished and moral suasion should be used by the Commissioner when it is necessary.

Generally speaking, we think that the Banking Bill is basically an improvement of the present legislation. The proposed amendments are, by and large, proper, valid and justified. We trust that upon enactment of the Bill, the banking industry will be better supervised and the interests of depositors better protected, though need for possible changes in some of the areas are still pressing.

However, the major implication of the Bill would be that smaller local banks will be in a more difficult position to compete with foreign institutions. Given the fact that six local banks have already run into troubles and have to be bailed out in one way or another, there will be no surprise that more smaller local banks will be acquired by so-called "Big Daddy" or merge with each other in order to survive. A restructuring in the banking sector appears to be inevitable and we earnestly hope that Hong Kong will further develop into a more sophisticated international financial centre.

APPENDIX 1

COMPARATIVE TABLE OF BANKING BILL AND ORDINANCE

Banking Bill	*Banking Ordinance (Cap. 155.)*	*Deposit-taking Companies Ordinance (Cap. 328.)*
PART I:		
PRELIMINARY		
Cl. 1—*NEW*		
Cl. 2(1)—"authorized institution"—*NEW*		
"capital to risk assets ratio"—*NEW*		
"company"—*MODIFIED*	s. 2(1)	
"controller"—*NEW*		
"deposit"—*MODIFIED*		s. 2(1)
"liquidity ratio"—*NEW*		
Cl. 2(2)		s. 2(2)
Cl. 2(3)	s. 2(1A)	
Cl. 2(4)—*NEW*		
Cl. 3(1) and (2)—*MODIFIED*		s. 3
Cl. 3(3), (4) & (5)	s. 57	
PART II:		
APPOINTMENTS, FUNCTIONS OF COMMISSIONER, REPORTS BY COMMISSIONER AND POWER OF GOVERNOR TO GIVE DIRECTIONS		
Cl. 4	s. 3	
Cl. 5—*MODIFIED*	s. 3	ss. 4 & 5
Cl. 6	s. 4	
Cl. 7—*NEW*		
Cl. 8	s. 4A	
Cl. 9—*NEW*		
Cl. 10—*MODIFIED*	s. 4B	s. 3B
PART III:		
BANKING BUSINESS AND BUSINESS OF TAKING DEPOSITS TO BE CARRIED ON BY AUTHORIZED INSTITUTIONS ONLY		
Cl. 11	ss. 5 & 61(1)	
Cl. 12(1), (2) & (3)		s. 6(1), (1A) & (1D)
Cl. 12(4)	s. 5A(2)	
Cl. 12(5) & (6)		s. 6(1E) & (2)
Cl. 12(7)		s. 26
Cl. 12(8)		s. 6(3)
Cl. 13		s. 35
Cl. 14(1), (2), (3), (4), (5) & (6)		s. 8
Cl. 14(7)		s. 26

Bill	*Banking Ordinance (Cap. 155.)*	*Deposit-taking Companies Ordinance (Cap. 328.)*
PART IV:		
LICENSING AND REGISTRATION OF AUTHORIZED INSTITUTIONS AND KEEPING OF REGISTER		
Cl. 15	s. 6	
Cl. 16	ss. 7 & 63(5)	
Cl. 17	ss. 7A & 63(5)	
Cl. 18	s. 8	
Cl. 19	s. 12(1) & (2)	
Cl. 20		s. 9(1), (2), (3) & (4)
Cl. 21(1)—*MODIFIED*		s. 10(1)
Cl. 21(2), (3), (4) & (5)		s. 10(2), (3), (6) & (7)
Cl. 21(6)		s. 34(1)(*a*) & (3)(*a*)
Cl. 21(7)	s. 63(5)	
Cl. 22	ss. 7A & 63(5)	
Cl. 23		s. 11(1) & (2)
Cl. 24(1)		s. 16A(1)
Cl. 24(2)—*MODIFIED*		s. 16A(2)
Cl. 24(3), (4) & (5)		s. 16A(3), (4) & (5)
Cl. 24(6)	s. 6(3)	
Cl. 25(1), (2), (3) & (4)		s. 16B(1), (2), (3) & (4)
Cl. 25(5)		s. 34(2)(*a*) & (3)(*b*)
Cl. 25(6)		s. 16B(5)
Cl. 26		s. 16C(1) & (2)
Cl. 27—*MODIFIED*		ss. 12 & 16D
Cl. 28(1)—*MODIFIED*		ss. 13(3) & 16E(3)
Cl. 28(2), (3), (4), (5) & (6)—*NEW*		
PART V:		
REVOCATION OF LICENCE OR REGISTRATION OF AUTHORIZED INSTITUTION		
Cl. 29	s. 9	
Cl. 30—*MODIFIED*	s. 11	
Cl. 31(1)—*MODIFIED*		s. 14(1)
Cl. 31(2)		s. 14(2)
Cl. 31(3)		s. 34(1)(*b*) & (3)(*a*)

Bill	*Banking Ordinance (Cap. 155.)*	*Deposit-taking Companies Ordinance (Cap. 328.)*
Cl. 32(1)—*MODIFIED*		s. 16F(1)
Cl. 32(2)		s. 16F(2)
Cl. 32(3)		s. 34(2)(*b*) & (3)(*b*)
Cl. 33(1)		s. 47
Cl. 33(2)—*MODIFIED*		ss. 44 & 48(1)
Cl. 33(3)		s. 48(2)
PART VI:		
SUSPENSION OF DEPOSIT-TAKING COMPANY		
Cl. 34		s. 43
Cl. 35		s. 45
Cl. 36(1) & (2)—*MODIFIED*		s. 46
Cl. 36(3)		s. 34(1)(*c*) & (3)(*a*)
Cl. 37		s. 47
Cl. 38		s. 48
PART VII:		
TRANSFER OF LICENCE OR REGISTRATION OF AUTHORIZED INSTITUTIONS		
Cls. 39 to 43 inclusive—*NEW*		
PART VIII:		
LOCAL BRANCHES, LOCAL REPRESENTATIVE OFFICES AND FEES		
Cl. 44	ss. 12A & 63(5)	ss. 16H & 34(1)(*d*) & (*f*)
Cl. 45	s. 12B(1) & (2)	s. 16I(1) & (2)
Cl. 46	ss. 12C & 66B	
Cl. 47	ss. 12D, 66, 66A & 66B	
Cl. 48(1) & (2)	s. 12E(1) & (2)	
Cl. 48(3)—*NEW*		
PART IX:		
OVERSEAS BRANCHES, OVERSEAS REPRESENTATIVE OFFICES AND FEES		
Cl. 49	ss. 12F & 63(5)	ss. 16J & 34(1)(*d*), (*e*), (*f*) & (*g*)
Cl. 50	ss. 12G, 63(5), 66 & 66A	s. 16K
Cl. 51	s. 12H(1) & (2)	s. 16L(1) & (2)

Bill	Banking Ordinance (Cap. 155.)	Deposit-taking Companies Ordinance (Cap. 328.)
PART X:		
POWERS OF CONTROL OVER AUTHORIZED INSTITUTIONS		
Cl. 52	ss. 13 & 65(2)	
Cl. 53	ss. 14 & 65(1)	
Cl. 54	s. 14A	
Cl. 55(1)—*MODIFIED*	s. 15(1)	
Cl. 55(2) & (3)	s. 15(2) & (3)	
Cl. 56	ss. 39, 63(6) & 66	
Cl. 57	s. 17	
Cl. 58	ss. 40 & 65(2)	
PART XI:		
AUDITS AND MEETINGS		
Cl. 59(1) & (2)	s. 36	
Cl. 59(3) & (4)—*NEW*		
Cl. 59(5)	s. 63(4)	
Cl. 60—*MODIFIED*	ss. 37, 63(5) & 65(4)	
Cl. 61—*NEW*		
Cl. 62—*NEW*		
PART XII:		
DISCLOSURE OF INFORMATION BY AUTHORIZED INSTITUTIONS		
Cl. 63	ss. 38, 63(8), 65(3) & (4)	s. 20
Cl. 64(1)—*MODIFIED*	s. 38A(1)	s. 20A(1)
Cl. 64(2), (3), (4), (5) & (6)	ss. 38A(2) & (3), 65(3), 66 & 66A	s. 20A(2), (3), (4) & (5)
Cl. 65(1)—*MODIFIED*	s. 33(1)	
Cl. 65(2)	s. 63(8)	
Cl. 66		s. 19(2) & (3)
Cl. 67	ss. 34 & 63(3)	s. 19A
Cl. 68	s. 39A	s. 31C
PART XIII:		
OWNERSHIP AND MANAGEMENT OF AUTHORIZED INSTITUTIONS		
Cl. 69	ss. 33(2) & (3) & 63(4)	

Bill	*Banking Ordinance (Cap. 155.)*	*Deposit-taking Companies Ordinance (Cap. 328.)*
Cl. 89	ss. 28 & 63(3)	
Cl. 90		s. 23C
Cl. 91		s. 23E(1)
Cl. 92	ss. 29 & 63(3)	
Cl. 93	s. 30	
Cl. 94		s. 24
Cl. 95	ss. 31 & 65(3)	
PART XVI:		
ADVERTISEMENTS, REPRESENTATIONS AND USE OF TITLE "BANK"		
Cl. 96		s. 27
Cl. 97		s. 28
Cl. 98		s. 29
Cl. 99—*NEW*		
Cl. 100		s. 21
Cl. 101	s. 67	
PART XVII:		
CAPITAL TO RISK ASSETS RATIO OF AUTHORIZED INSTITUTIONS		
Cls. 102, 103, 104 & 105—*NEW*		
PART XVIII:		
LIQUIDITY RATIO OF AUTHORIZED INSTITUTIONS AND MATTERS AFFECTING LIQUIDITY RATIO		
Cls. 106, 107, 108, 109 & 110—*NEW*		
PART XIX:		
UNINCORPORATED BANKS		
Cl. 111—*MODIFIED*	s. 42	
Cl. 112	s. 43	
Cl. 113	s. 44(1) & (2)	
Cl. 114	ss. 44A & 63(4)	
Cl. 115	s. 45	
Cl. 116	s. 46	
Cl. 117—*MODIFIED*	s. 47	
Cl. 118	ss. 48 & 63(6)	
Cl. 119	ss. 49 & 63(8)	
Cl. 120	s. 55A	

Bill	*Banking Ordinance (Cap. 155.)*	*Deposit-taking Companies Ordinance (Cap. 328.)*
PART XX:		
INVESTIGATIONS OF AUTHORIZED INSTITUTIONS		
Cl. 121	ss. 57A & 68A(2)	s. 38
Cl. 122	ss. 57B & 68A(1)	s. 39
PART XXI:		
MISCELLANEOUS		
Cl. 123	s. 50	
Cl. 124	ss. 53 & 60	s. 25
Cl. 125(1)—*MODIFIED*	s. 53A(1)	s. 25A(1)
Cl. 125(2) & (3)	s. 53A(2) & (3)	s. 25A(2)
Cl. 126(1), (2), (3) & (4)	s. 55	
Cl. 126(5) & (6)		s. 40
Cl. 127	s. 59	
Cl. 128	s. 62	
Cl. 129	s. 51	s. 32
Cl. 130	s. 58	
Cl. 131	s. 52(1)	s. 41(1)
Cl. 132	s. 41A	
Cl. 133	s. 41B	s. 24C(2) & (3)
Cl. 134		s. 30
Cl. 135	s. 54	
Cl. 136(1)	s. 35(1)	
Cl. 136(2)—*MODIFIED*	s. 6(2)(*a*)(ii)	s. 9(5)
Cl. 136(3)	s. 63(8)	
Cl. 137	s. 56	s. 36(1)
Cl. 138	s. 57C	s. 42
Cl. 139(1)		s. 37
Cl. 139(2) and (3)—*NEW*		
Cl. 140	s. 69	
Cl. 141—*NEW*		
PART XXII:		
TRANSITIONAL, SAVINGS AND REPEAL		
Cls. 142, 143, 144, 145, 146, 147, 148, 149, 150, 151, 152 & 153—*NEW*		
FIRST SCHEDULE		FIRST SCHEDULE
SECOND SCHEDULE		SECOND SCHEDULE
THIRD SCHEDULE, FOURTH SCHEDULE & FIFTH SCHEDULE—*NEW*		

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